Supreme Court, U.S.
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No. 87-1133

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

FIRST FEDERAL SAVINGS AND LOAN ASSOCIATION OF CLAREMORE, OKLAHOMA, AND GREAT PLAINS FEDERAL SAVINGS AND LOAN ASSOCIATION (FORMERLY CUSTER COUNTY FEDERAL SAVINGS AND LOAN ASSOCIATION) OF WEATHERFORD, OKLAHOMA,

Appellants,

v.

THE OKLAHOMA TAX COMMISSION OF THE STATE OF OKLAHOMA,

Appellee.

ON APPEAL FROM THE SUPREME COURT OF OKLAHOMA

MOTION TO DISMISS, OR IN THE ALTERNATIVE, MOTION TO AFFIRM

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QUESTIONS PRESENTED

Whether a state may tax interest income of a federally chartered savings and loan association earned from overnight/demand deposits maintained with a Federal Home Loan Bank and from bonds issued by Federal National Mortgage Association.

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Pursuant to Rule 16 of this Honorable Court, Appellee, Oklahoma Tax Commission, respectfully submits that this appeal should be dismissed, or in the alternative, that the decision of the Supreme Court of the State of Oklahoma should be affirmed. The questions presented to the Supreme Court of the State of Oklahoma was whether overnight/demand deposits of federally chartered savings and loan associations in a Federal Home Loan Bank and bonds issued by Federal National Mortgage Association are obligations of the United States and exempt from state tax under specific federal statutes, the supremacy clause, or under general constitutional principles. The Supreme Court of the State of Oklahoma held that interest income of the Appellants, federally chartered savings and loan

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associations, earned on overnight/demand deposits in the Federal Home Loan Bank is subject to taxation by the state relying upon *Hibernia Savings and Loan Society v. San Francisco*, 200 U.S. 310, 315 (1906); and, that interest income of the Appellants, federally chartered savings and loan associations, earned on bonds issued by Federal National Mortgage Association is subject to taxation by the state relying upon 12 U.S.C. §1719(b).

The decision of the Supreme Court of the State of Oklahoma is correct and consistent with the decisional law of this Honorable Court and federal statutes.

THE OPINIONS BELOW

1. The orders of the Oklahoma Tax Commission, Order No. 85-05-30-07 and Order No. 85-05-30-08 entered May 30, 1985, and Order Nunc Pro Tunc No. 85-05-30-39 correcting an inadvertent order numbering error, entered May 30, 1985, appear at pages B-1 through B-16 and C-1 through C-16 of the Appendices in the Jurisdictional Statement.

2. The Opinion of the Supreme Court of the State of Oklahoma, entered May 26, 1987, affirming the parts of the Orders of the Oklahoma Tax Commission which determined that interest income from overnight/demand deposits in a Federal Home Loan Bank and bonds issued by Federal National Mortgage Association is subject to state taxation, appears at pages A-1 through A-19 of the Jurisdictional Statement.

THE PARTIES

The Oklahoma Tax Commission is the Appellee and by state statute, Section 105 of Title 68 of the Oklahoma Statutes, is authorized to represent the interests of the State of Oklahoma in this case.

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STATEMENT OF JURISDICTION

Appellants, before the Oklahoma Tax Commission and the Oklahoma Supreme Court, challenged the application of the State income tax to interest income received by Appellants from overnight/deposits in a Federal Home Loan Bank and bonds issued by Federal National Mortgage Association. Appellants did not attack the validity or constitutionality of a state statute but rather attacked the administration of a state statute. Likewise, Appellants, in the Jurisdictional Statement, challenge the application of a state statute.

Appellants assert that 28 U.S.C. §1257(2) confers jurisdiction upon this Honorable Court to review the decision of the Oklahoma Supreme Court. 28 U.S.C. §1257(2) states:

> "§1257. State courts; appeal; certiorari
>
> Final judgments or decrees rendered by the highest court of a state in which a decision could be had, may be reviewed by the Supreme Court as follows:
>
> (2) By appeal, where is drawn in question the validity of a state statute of any state on the ground of its being repugnant to the Constitution, treaties or laws of the United States, and the decision is in favor of its validity."

The state statute involved is Subsection (A) (2) of 2358 of Title 68 of the Oklahoma Statutes. Subsection (A) (2) of Section 2358 states:

> A. Taxable income and, where use of adjusted gross income is necessary, i.e., required by this act, adjusted gross income shall be adjusted as follows to arrive at Oklahoma taxable income and Oklahoma adjusted gross income:
>
> 2. There shall be deducted amounts included in such income amounts that the state is prohibited

> from taxing because of the provisions of the Federal Constitution, the State Constitution, federal laws or laws of Oklahoma...

Appellants, for the first time on appeal, assert that the state statute involved is Subsection (C) of Section 2355 of Title 68 of the Oklahoma Statutes. Section 2355, Subsection (C), imposes the state income tax upon the income of corporations. Section 2358 specifies the income, deductions, exemptions and allocations to arrive at the income upon which the levy is imposed. Neither the validity of Section 2355 nor Section 2358 was challenged below.

To sustain a challenge of a state statute as repugnant to the Constitution or laws of the United States, the challenge must be distinct and substantial. *House v. Road Improvement District No. 2 of Conway County, Arkansas*, 45 S.Ct. 60 (1924). Appellants attacked only the administration of the state income tax statutes and may not now, on appeal, attack the state statutes as the basis for jurisdiction under 28 U.S.C. Section 1257 (2). *McColdrick v. Compagnie Generale Transatlantique*, 60 S.Ct. 670, 672 (1940).

The issue jointly presented to the administrative tribunal, Appellee, Oklahoma Tax Commission, by counsel for the federally chartered savings and loan associations and the Income Tax Division, was whether interest income from the specified sources is exempted from state taxation by federal law and Subsection (A)(2) of Section 2358 of Title 68 of the Oklahoma Statutes. Appendices to Jurisdictional Statement, pages B-1, C-1 and C-2. That same issue was presented to and decided by the Oklahoma Supreme Court. The argument made by Appellants in the Jurisdictional Statement that the inclusion of interest income in the calculation of taxable income is violative of constitutional and statutory provisions does not draw into question the validity of a

state statute as repugnant to the Constitution and statutes of the United States. The Administrative Orders of the Appellee are questioned in this case, not state statutes.

The Administrative Orders, affirmed in part by the Oklahoma Supreme Court, are judicial in nature. An administrative order may be considered as a statute for jurisdictional purposes under 28 U.S.C. §1257(2) if it is legislative in nature. *Hamilton v. Regents of the University of California*, 55 S.Ct. 197 (1934). In *Hamilton*, an order was issued by a land grant state university requiring compulsory military training. The Court, in finding that the order was indeed a statute as applies to "statute of any state" Section 1257 (2) stated:

> The assailed order prescribes a rule of conduct, and applies to all students belonging to the defined class. . . . The meaning of 'Statute of any State is not limited to acts of state Legislatures. It is used to include every act levislative in character to which the state gives sanction, no distinction being made between acts of the state Legislature and other assertions of the state lawmaking power.
>
> 55 S.Ct., at p. 202.

In *Lathrop v. Donohue*, 81 S.Ct. 1826 (1962), this Court considered whether an order of the Wisconsin Supreme Court integrating the Wisconsin Bar was a statute within the meaning of §1257 (2). In finding the Wisconsin order to be legislative rather than adjudicatory in nature, the Court stated:

> Integration of the Bar in Wisconsin bore no resemblance to adjudication. . . (T)he court sought to regulate the profession by applying its orders to all present members of the Bar and to all persons coming within the described class in the future. As such, the action had the characteristics of legislation.

81 S.Ct., at page 1829.

In the case at bar, the Administrative Orders are adjudicatory in nature, issued in individual taxpayer protest proceedings. The Administrative Orders do not prescribe rules of conduct as in the *Hamilton* and *Lathrop* cases. The Orders were issued based upon the evidence and particular facts presented in an adversarial proceeding.

Further, even the Questions presented at page i of the Jurisdictional Statement do not draw into question the validity of a state statute.

In a recent decision, *Rockford Life Insurance Company v. Illinois Department of Revenue,* ___ S.C. ___ (1987), 55 L.W. 4747 (1987), decided June 8, 1987, this Court, at footnote 3, noted that its jurisdiction is mandatory under Section 1257(2). In the *Rockford Life Insurance Company* case, an Illinois statute was challenged. The Illinois taxing authorities included the value of Ginnie Mae Mortgage-Backed Securities in calculating net assets for state property taxes pursuant to statute. That statute was subsequently repealed. Although the constitutional challenge and arguments of *Rockford Life Insurance Company* are practically identical to those propounded by Appellants herein, this case does not attack the validity of a state statute.

WHEREFORE, Appellee respectfully submits that Appellants failed to establish a jurisdictional basis for review by this Honorable Court of the decision rendered by the Supreme Court of the State of Oklahoma on May 16, 1987.

THE QUESTION PRESENTED FOR REVIEW

The Supreme Court of the State of Oklahoma decided that overnight/demand deposits of federally chartered savings and loan associations in a Federal Home Loan

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Bank and bonds issued by Federal National Mortgage Association were not obligations of the United States and thus, interest income received by the federally chartered savings and loan associations from those sources is subject to non-discriminatory state taxation as authorized in 12 U.S.C. §1464(h). *Sooner Federal Savings and Loan Association v. Oklahoma Tax Commission*, 662 P.2d 1366 (Okl. 1982) app. dism'd, 103 S.Ct. 1760 (1983).

The question on review presented by Appellants is whether the imposition of a state tax upon interest income received by federally chartered savings and loan associations from overnight/demand deposits in a Federal Home Loan Bank and Federal National Mortgage Association bonds violates the borrowing clause and the supremacy clause of the United States.

STATEMENT OF THE CASE

This appeal does not attack the validity of a state statute. Rather, Appellants claim a tax exemption from state income tax under federal and state statutes, 12 U.S.C. Section 1433 and Subsection (A) (2) of Section 2358 of Title 68 of the Oklahoma Statutes, and the principle of governmental immunity.

The case arose out of office audit assessments of state corporate income tax which were protested by Appellants pursuant to Oklahoma's Uniform Tax Procedure and, more specifically, 68 O.S. 1981, §221. The facts and evidence presented in the administrative proceeding were stipulated and are set out at pages B-3 through B-7 and C-2 through C-5 in the Appendices to the Jurisdictional Statement. Based upon the stipulated facts and evidence, the Oklahoma Tax Commission, in the Administrative Orders, concluded that interest income earned on overnight/demand deposits in the Federal Home Loan Bank, Topeka, Kansas, is income

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earned on the property of the savings and loan association and is not income of the Federal Home Loan Bank exempted from state taxation by 12 U.S.C. Section 1433, (pages B-13 and C-9, Appendices to Jurisdictional Statement); and that interest income earned on bonds issued by Federal National Mortgage Association is income earned on the property of the savings and loan associations (pages B-13 and B-14 and C-9, Appendices to Jurisdictional Statement). These conclusions contained in the Administrative Orders were affirmed by the Oklahoma Supreme Court.

APPELLEE'S ARGUMENT IN SUPPORT OF MOTION TO DISMISS, OR IN THE ALTERNATIVE, MOTION TO AFFIRM

The issue presented is not novel or one of first impression. Neither the federal nor the state courts are divided on the issue. This case does not present a substantial, important or unsettled question of federal law. Furthermore, the case does not arise under the mandatory jurisdiction of 28 U.S.C. §1257(2).

The sub-issues of the question presented are directly answered by federal statute or decisional law of this Court, to-wit:

1. What income of a federally chartered savings and loan association may be taxed by the states? 12 U.S.C. §1464 permits state taxation of all the income of a federally chartered savings and loan association. *First Federal Savings and Loan Association of Boston v. State Tax Commission*, 437 U.S. 255 (1978);

2. Is an overnight/demand deposit account in a Federal Home Loan Bank an obligation of the United States? 12 U.S.C. §1435 declares obligations of the Federal Home Loan Banks are not obligations of the United States.

3. Is a bond issued by Federal National Mortgage Association an obligation of the United States? 12 U.S.C. Section 1719(b) declares obligations of Federal National Mortgage Association are not obligations of the United States.

4. Is income distributed by a Federal Home Loan Bank to its member savings and loan associations exempt from state taxation by 12 U.S.C. §1433? 12 U.S.C. §1433 exempts the income of the Federal Home Loan Bank from taxation by the states but does not exempt income distributed to its member savings and loan associations. *Sooner Federal Savings and Loan Association v. Oklahoma Tax Commission*, 662 P.2d 1366 (Okl. 1982), appeal dism'd 103 S.Ct. 1760 (1983).

5. Are overnight/demand deposits in a Federal Home Loan Bank and bonds issued by Federal National Mortgage Association obligations of the United States immune from state taxation under 31 U.S.C. §3124, formerly 31 U.S.C. §742? This Court has defined an obligation of the United States protected from state taxation as a credit instrument characterized by a written document, bearing interest, which has a binding promise of the United States to pay specified sums at specified dates and which is issued pursuant to specific Congressional authorization and pledges the full faith and credit of the United States in support of the promise to pay. *Smith v. Davis*, 323 U.S. 111 (1944); *Hibernia Savings and Loan Association v. San Francisco*, 200 U.S. 310 (1906). The federal statutes, 12 U.S.C. §1324 and 12 U.S.C §1719, prevent the involved assets of the Appellants, federally chartered savings and loan associations, from being declared obligations of the United States. In *Rockford Life Insurance Co. v. Illinois Department of Revenue*, ___ S.Ct. ___ (1987), this Court found the guarantee of the United States to pay the mortgage-backed securities guaranteed by Government National Mortgage Association too remote

to meet the test of *Smith v. Davis*, supra. This case does not present a question of state taxation of even a remote obligation of the United States.

The decisions of this Court and the federal statutes have settled all aspects of the issue of this case. The decision of the Oklahoma Supreme Court is consistent with 12 U.S.C. §1464(h) which permits state taxation of federally chartered savings and loan associations, with 12 U.S.C. 1435 and 1719 which declare that obligations of a Federal Home Loan Bank and Federal National Mortgage Association are not obligations of the United States, and with the decisions of this Court in *Smith v. Davis*, 323 U.S. 111 (1944); *Hibernia Savings and Loan Society v. San Francisco*, 200 U.S. 310 (1906); *Memphis Bank & Trust Co. v. Garner*, 459 U.S. 392 (1983); *Metropolitan Life Insurance Co. v. Ward*, 470 U.S. 869 (1985); and *Rockford Life Insurance Company v. Illinois Department of Revenue*, ___ S.Ct. ___ (1987).

The interest income taxed by the decision of the Oklahoma Supreme Court is income of the Appellants. Upon distribution of that income to Appellants, the individual owners, Appellants, may be taxed. *Tax Film Corporation v. Doyal*, 286 U.S. 123 (1932).

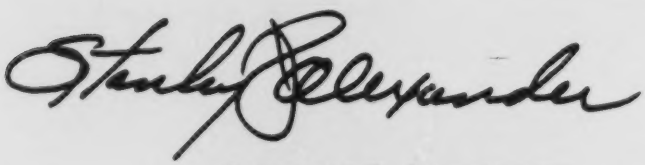
WHEREFORE, Appellee respectfully requests that this Honorable Court dismiss the appeal of Appellants for the reasons that this case does not draw into question the validity of a state statute which has been decided in favor of its validity. Neither does this case present a substantial, unsettled question of federal law. In the alternative, the decision of the Supreme Court of the State of Oklahoma, with clarity and reason, applies the federal statutory and decisional law of governmental immunity to precise aspects of the law and should be affirmed by this Court.

CONCLUSION

Appellee respectfully submits that state taxation of interest income to Appellants, federally chartered savings and loan associations, from overnight/demand deposits in the Federal Home Loan Bank and bonds issued by Federal National Mortgage Association does not violate the borrowing clause or the supremacy clause of the Constitution of the United States. Appellee further submits that this appeal should be dismissed for want of jurisdiction under 12 U.S.C. §1257(2) and for want of a substantial, unsettled federal question.

Respectfully submitted,

OKLAHOMA TAX COMMISSION



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CERTIFICATE OF MAILING

This is to certify that a true and correct copy of the above and foregoing Motion to Dismiss, or in the Alternative, Motion to Affirm, was mailed, postage prepaid, on the 3rd day of February, 1988, to the following:

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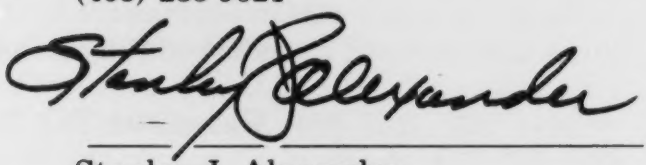

Stanley J. Alexander